The optimal level of public expenditure

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Abstract
The budgeting process consists of sharing the adoption of the budgeting decision between the levels and parties involved in the budgeting, while defining for each participant the competencies and deadlines to ensure the budgeting is performed in due time.
The budgeting process is part of the budgeting procedure which also involves the budget implementation, closing and control.
The State budget, acting as main financial plan of the State and being vested with the quality to predict, must essentially provide answer to three questions:
- which are the public goods and services that the State must put at its citizens’ disposal free of charge?
- who shall bear their financing expenditure and from what sources?
- which shall be the consequences on the overall economic balance and the international financial relationships of the respective State?

Key words: budget, budgetary deficit, budgeting procedure, optimizing public expenditure, current economic crisis.

1. Introduction
Nowadays, considering that the budgets of the last years have fallen into deficit, an extremely complex problem that arises is the size of the public sector and the solution to this problem should offer the answer to the question: which should be the level of government activity?
In each State’s economy, governmental public expenditure is carried out with a view to producing goods and services which are, generally, offered to citizens free of charge. This is the case of health and education services. In the private sector, consumers may satisfy all their needs by means of the market, while producers offer much more products. In the non-market public sector, however, the mechanism based on this supply and demand game does not usually function. The level of the service stocks is decided by the political process and not by the market. Of course, this means that it is possible for the politically-determined offer to be either too small or too big as compared to the national economic optimum.

2. Problem formulation
2.1. Substantiating the issue
A public good, sometimes called public consumption good, is the good for which the total production cost does not increase together with the total number of consumers. The expenditure on national defense is the classic case: an army of a given size protects all of a country's citizens, irrespective of their number, e.g. 22 million, 50 million or 100 million citizens. Another relevant example is public order: a visitor enjoys the crime-free streets of a city as much as the citizens of that respective town[1].

Information is a also public good. Other public goods are: the power plants, the weather forecasts as type of information, the fresh air reserve, the open air concerts, etc.

It is important for a public good, once produced, to become available to all of us, being impossible for those who are willing to pay for it to restrict its use.

2.2. Public characteristics of the goods
Public goods have two distinct characteristics: 
- the non-rivalry and the non-excludability

The non-rivalry means that the amount consumed by a person should not influence the quantity that other people can consume. For instance, if ten boats enter a channel under guidance from a lighthouse, this should not diminish the services obtained from the lighthouse by an eleventh boat entering that respective channel. On the contrary, the consumption of a private-owned bread by a person means that the bread under discussion can no longer by consumed by another person.

The non-excludability means that once a public good is produced, there is no way to stop someone from consuming it. In the above example, the non-excludability consists of the fact that the lighthouse spreads its light at the entrance to the port for all the ships in the area. Another example, even more relevant, is national defense. A national army defends all of a country's citizens no matter if they paid their taxes or not[2]. The State cannot refuse armed protection in case of armed conflict to citizens that have not paid their taxes.

All public goods are commonly consumed, meaning that once they are offered, all citizens benefit from them whether or not they have paid their taxes.

Authentic public goods such as the national defense system, the justice system and the public order system must as a rule be offered by means of the political process and not by means of the market, part of the taxes having been, of course, paid.

One of the controversial ideas says that public goods such as the health and education services should be offered free of charge by the State or for good and valuable consideration by means of the markets. The possibility for people to rationally spend more on health and education services than what the political process establishes exists, of course, if only there was a way for them to voice their preferences. The determination of the public sector optimal size involves the analysis of the public expenditure growth and of the overall budgeting process.

3. Problem solution
3.1. Models of public option develops
Economic theory also analyses the budgeting process from the viewpoint of the public option. The analysis is performed with the help of a conceptual and analytical apparatus of the microeconomic theory, namely the theory of public option. The theory of public option is a microeconomic government theory based on the assumption of the individual rationality.

With respect to the budgeting process, the theory of the public option develops two models:
- the model of the legislative demand;
- the model of the agent offer.

According to the model of the legislative demand, the budgeting decisions of the political commission depend on:
- the individual demand for public services coming from each politician that is part of the commission;
- the nature of the dominated negotiation;
- the coalition forming process.

Normally and naturally, in a representative type of democracy, the individual demand of the politician is supposed to be linked to the demand from the citizens (the electors). However, the individual demand of the politician (the elected politician) depends on preferences, on the taxes that diminish the fortune and revenues of that respective politician’s electors and, especially, on the ones of the politician him/herself.

The model of the agent offer (the institution) focuses on the tax for public services under the circumstances of a given policy demand. According to this model, the taxes are established by bureaucrats who hold authority

over the public goods production. The public goods production depends on the services’ production cost, the demand of services from the part of politicians, the structure of the domestic market used by bureaucrats to sell the services to politicians and on bureaucrats’ objectives.

In order to correctly interpret the data regarding the dynamics of the public expenditure, it is necessary to build models capable of using the whole of the economic, political and social factors, which influence public expenditure and its growth.

Such influences of the above mentioned factors are to be found in the macro-models of public expenditure growth[3].

The following three models are even better known in the economic doctrine:
1. models for the development of the public expenditure growth;
2. Adolf Wagner’s model – Wagner’s law;
3. Peacock and Wiseman’s model (classical style).

3.2. The model for the development of the public expenditure growth

The models of Musgrave and Rostow are generalizations obtained as a result of examining a big number of different cases of national economy development.

At the beginning of the economic growth and development, public sector investments and their weight in the total economic investments were considered as big.

The main objective of the public sector was to ensure the special global infrastructure, such as: the roads, the transportation system, the sewage system, obeying law and order, the health and education as well as other human resources investments.

The continuous growth of the public investments was motivated by the fact that economy had to adapt to the dynamics of the progress towards the middle stages of the social-economic development.

During this stage of development of the economic growth, the executive continues to ensure the funds needed for the public investments; at the same time, these complement the growth of the private investments.

In all stages of the human society development, market failures exist and may prevent the jump to the next level of development and maturity.

Based on this idea, the growth of the government involvement is supported both theoretically and practically as opposed to the market failures[4].

R. A. Musgrave advances the idea that, subsequent to the development period, while total investments - as percentage from the Gross Domestic Product (Gross National Product) - grow, the percentage of public sector investments from the GDP decreases.

W.W. Rostow argues that once the economy reaches the maturity stage, the prevalence of the public expenditure shall turn from public expenditure for infrastructure purposes into increased public expenditure in the educational, health and social security sectors.

3.3. Wagner’s Model (Law)

In most of the industrial countries, governments use the periods of peace to plan the growth of their expenditure on goods and services; in this way, they generally maintain a constant proportion from the national income. This practice has been called granting the permanent income to government consumption, since the growth of the real government consumption is planned based on the growth trend of the real national income.

This means that the percentage of government expenditure from the national income grows when this one is below the trend level and diminishes when the national income exceeds this level.

This proportionality between the State activity and the national income has been noticed more than one century ago by the economist Adolf Wagner (1835-1917). Wagner’s preoccupation was to explain the GNP part attributed to the

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public sector. The conclusions of the German economist have taken the form of the model known as Wagner's Law and defined by the author himself as 'a law of the rising expansion of the public activities and especially of the State'.

Wagner’s statement was misinterpreted; thus, he was supposed to have claimed that public activity endlessly grows as proportion of the national activity. Wagner underlined that his model can be transformed into a ‘law of the rising financial needs of the State and of the self-governing bodies’. This way of phrasing his idea does not clearly indicate whether the German economist meant the growth of the public expenditure from the GDP or the GNP, in other words the relative growth of the public sector, or if he thought about the absolute size of the public sector.

Considering the model of R. Musgrave, which says that while the proportion of the total investments from the GDP (GNP) grows, the proportion of the public sector investments from the GDP diminishes, one may consider that Wagner’s law is an expression of the growth of the public sector’s relative size. Wagner’s real statements were that, following an increase in the public activity proportion, in the development stage of the economy, there is a maximum proportion of the public activity from the national economy and this proportion shall not be continuously exceeded. This is why there is a certain proportion between the public expenditure and the national income, which shall not be continuously exceeded. This fact only confirms the rule that says there should be a certain balance between individuals’ expenses incurred to satisfy their various needs. The State’s fiscal needs covered by taxes stand as elements of expenditure in the budget of the citizens' households.

Although based on many realistic opinions, Adolf Wagner’s model carries the disadvantage that it is not based on a well-grounded theory of the public option. The German economist presented his own law, leaving aside the issues of the public option, and phrased an organic theory of the State. In his model, the State was supposed to act as if it were an entity that is capable of decision-taking, independently of the society members.

One of the main constrains on the government ability to increase the level of the services offered is the acceptable taxation level needed to finance these services. The irony is that the citizens from a developing economy might rationally choose to spend an increasingly greater proportion of their revenue on health and education if the right choice mechanism would be available for them, but it is also possible that the political process does not manage to deliver the required production.

3.4. The models of Peacock and Wise
A. T. Peacock and J. A. Wiseman’s study is one of the best-known analyses of the public expenditure dynamics from the economic doctrine.

The two authors created their model based on a political theory of the public expenditure according to which the executive power must take into account the wishes of its citizens not to pay high taxes and to benefit from increasingly important public services. Citizens' resistance to taxes is permanent and faces periods and moments of recrudescence. A latent resistance is almost always present and may be doubled by one organized by citizens negotiating with the administration.

Based on the idea that the tax is too high as compared to what the political-administrative State apparatus and the decentralized collectivities may offer them and that, contrary to the theory, the taxes do not embody the price for the services provided by the public apparatus, the two economists saw the voter as an individual who enjoy the advantages of the public goods and services, but who does not like to pay taxes. They assumed the existence

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of a tolerable tax level which acts as a coercion element on government behavior. Peacock and Wiseman saw taxation as having influence on the public expenditure. Thus, when economy and income grow at equal pace, taxes also grow in parallel at steady tax rates, and this makes it possible for the public expenditure to grow at the same pace as the GDP.

The case in which, in periods of crisis and war, the private expenditure is transferred to the public expenditure was called by them 'the transfer effect'.

The normal growth of the public expenditure as a general tendency is disrupted by periods of economic crisis, starvation, or natural calamities, which as a rule impose a much more rapid growth of the public expenditure. After economies come out of the crisis, in the period immediately following, the public expenditure no longer returns to the initial level from before the crisis or war period. Wars have never been supported exclusively from taxes since no State has this kind of tax capacity. Wars have also been financed from loans assumed by governments and put up with in the following periods.

The two authors have also defined 'the inspection effect'. According to the two economists, this effect originates in voters’ increased vigilance and monitoring of the government with respect to the social problems in periods of economic transition.

The government is obliged to explain the governing program to voters; the main objective of this program is, generally, the present or future improvement of the social conditions, which makes it easier to put up with a higher tax level brought about by the public consumption and the existing debts.

Although along the years, Peacock and Wiseman’s model has been subject to critics, in today’s times, the phenomenon of the public expenditure growth and the tax burden in periods of crisis can be also be very well interpreted.

4. Conclusion
The budget resource demands are usually bigger than the availabilities for their satisfaction.

The administrative institutions – ministers, but also other internal and external proprietary units are entitled to budgetary allocation pretensions.

Based on the idea that, in order to come out of the actual crisis it faces, Romanian society must adopt the model that is followed by human society in general, namely the information, competitive, ecological and social society, under the current economic circumstances, the shaping of the State budget expenditure also requires new solutions to be adopted or old models to be adapted.

References:


